

Message Text

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SP-02 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-07
CEA-01 DODE-00 PM-05 H-02 L-03 PA-02 /115 W
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P 250240Z MAY 78
FM AMEMBASSY OTTAWA
TO SECSTATE WASHDC PRIORITY 7487
INFO AMEMBASSY BONN
AMCONSUL CALGARY
AMCONSUL HALIFAX
AMCONSUL MONTREAL
AMCONSUL QUEBEC
AMCONSUL TORONTO
AMCONSUL VANCOUVER
AMCONSUL WINNIPEG

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DEPT. PASS CEA, TREAS, FRB

E.O. 11652:N/A
TAGS: ECON, CA
SUBJECT: ECONOMIC DEVELOPMENTS: WEEK ENDING MAY 19.

1. SUMMARY: GOC HAS TABLED IN PARLIAMENT ITS PROPOSED REVISIONS TO THE BANK ACT (OTTAWA 2571). PRELIMINARY FIGURES SHOW NARROWING OF CANADIAN AUTO TRADE DEFICIT WITH THE U.S. IN FIRST QUARTER IN 1978. PRICE PERFORMANCE HAS SHOWN IMPROVEMENT. WAGE INCREASES CONTINUED TO MODERATE IN FIRST QUARTER AND INCREASE IN CONSUMER PRICES DECELERATED IN APRIL DESPITE RAPID ADVANCE IN FOOD PRICES (OTTAWA 2540). INDUSTRIAL PRODUCTION WAS STAGNANT IN MARCH, BUT OUTLOOK FOR PRODUCTION IMPROVED AS MANUFACTURERS' SHIPMENTS, NEW ORDERS AND UNFILLED ORDERS INCREASED IN MARCH, WHILE
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INVENTORIES DECLINED. CONSUMER CREDIT OUTSTANDING ROSE IN MARCH. GROWTH OF AFTER TAX PROFITS DECLINED IN FIRST QUARTER. CANADIAN DOLLAR EXCHANGE RATE CONTINUES FIRM. CENTRAL BANK GOVERNOR SAID CURRENT ACCOUNT DEFICIT MIGHT BE SMALLER THIS YEAR THAN LAST. SHORT TERM INTEREST RATES CONTINUED TO FALL IN WEEK; BOND PRICES ROSE. EASING OF CONDITIONS IN DOMESTIC CAPITAL MARKETS COULD BE TEMPOR-

ARY. COST OF CANADIAN BORROWING IN EUROPEAN MARKETS
LIKELY TO RISE. END SUMMARY.

2. BANK ACT: GOC HAS TABLED IN PARLIAMENT ITS PROPOSED
REVISIONS TO BANK ACT. LEGISLATION FOLLOWS 1976 WHITE
PAPER IN PERMITTING THE ESTABLISHMENT (ALBEIT WITH RESTRIC-
TIONS) OF FOREIGN BANKS. OTHER PROPOSALS WOULD ALLOW GREATER
PROVINCIAL PARTICIPATION IN BANKING, EXEMPT NON-BANK
FINANCIAL INSTITUTIONS FROM RESERVE REQUIREMENTS AND
AUTHORIZE CANADIAN CHARTERED BANKS TO ENGAGE IN FACTORING
AND LEASING (SEE OTTAWA 2571).

3. AUTO TRADE: ACCORDING TO PRELIMINARY UNOFFICIAL
STATCAN FIGURES, CANADIAN AUTO TRADE DEFICIT WITH THE U.S.
WAS CDOLS 69.3 MILLION IN FIRST QUARTER OF THIS YEAR,
COMPARED WITH CDOLS 158.9 MILLION IN FIRST QUARTER OF 1977.
TOTAL AUTOMOTIVE EXPORTS AVERAGED CDOLS 2.5 BILLION IN
FIRST QUARTER, UP CDOLS 208 MILLION FROM FIRST QUARTER
1977, WHILE IMPORTS ROSE CDOLS 118 MILLION TO CDOLS 2.6
BILLION. PARTS DEFICIT ROSE BY CDOLS 45.8 BILLION TO
CDOLS 754.6 MILLION; SURPLUS ON ASSEMBLED VEHICLES IN-
CREASED BY CDOLS 135.5 MILLION TO CDOLS 685.3 MILLION.

4. WAGES: AVERAGE ANNUAL INCREASE IN BASE WAGES OF NEW
SETTLEMENTS IN COLLECTIVE AGREEMENTS DURING THE FIRST
QUARTER WERE 6.7 PERCENT COMPARED WITH 7.1 PERCENT IN
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FOURTH QUARTER OF 1977. OF THE 103 MAJOR SETTLEMENTS IN
FIRST QUARTER, SIXTY SEVEN ONE-YEAR AGREEMENTS PROVIDED
FOR A 6.6 PERCENT WAGE INCREASE; THIRTY ONE TWO-YEAR
AGREEMENTS ACCORDED AN INCREASE OF 7.6 PERCENT IN THE
FIRST YEAR AND 6.6 PERCENT IN THE SECOND; FIVE THREE-YEAR
AGREEMENTS PRODUCED YEARLY INCREASES OF 11.3 PERCENT,
6.7 PERCENT AND 5.3 PERCENT RESPECTIVELY. NEGOTIATED WAGE
INCREASES IN FIRST QUARTER WERE LOWEST SINCE FOURTH
QUARTER OF 1972.

5. ECONOMIC INDICATORS:

-- INDEX OF INDUSTRIAL PRODUCTION (SA) WAS STAGNANT IN
MARCH AT FEBRUARY LEVEL OF 126.1. SMALL INCREASE (0.5
PERCENT) IN MANUFACTURING OUTPUT WAS OFFSET BY DECLINE IN
MINE AND MINERALS PRODUCTION. IN FIRST QUARTER OF 1978,
INDUSTRIAL ROSE AT SEASONALLY ADJUSTED AVERAGE ANNUAL RATE
OF ONLY 0.32 PERCENT.

-- STATCAN SURVEY INDICATES THAT AFTER TAX CORPORATE
PROFITS WERE CDOLS 2.4 BILLION IN FIRST QUARTER OF 1978,
A 9.9 PERCENT INCREASE OVER FIRST QUARTER 1977. PROFITS

IN MANUFACTURING SECTOR ADVANCED BY 8.4 PERCENT; MINING PROFITS WERE DOWN BY 1 PERCENT. SLOW GROWTH OF PROFITS, BARELY MORE THAN INFLATION, REFLECTS WEAK DOMESTIC DEMAND AND VIRTUAL STAGNATION OF INDUSTRIAL PRODUCTION.

-- VALUE OF MANUFACTURERS' SHIPMENTS WAS CDOLS 9.81 BILLION IN MARCH, UP 0.1 PERCENT FROM REVISED FEBRUARY

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TOTAL OF CDOLS 9.80 BILLION. DURABLE GOODS SHIPMENTS DECLINED BY 1.1 PERCENT, WHILE SHIPMENTS OF NON-DURABLES ROSE BY 1.0 PERCENT. NEW ORDERS INCREASED BY 1.5 PERCENT TO CDOLS 10.3 BILLION IN MONTH, WHILE UNFILLED ORDERS ADVANCED BY 4.1 PERCENT TO CDOLS 11.2 BILLION. VALUE OF OWNED INVENTORY FELL BY 0.4 PERCENT TO CDOLS 18.8 BILLION; RATIO OF INVENTORIES TO SHIPMENTS WAS 1.92:1 IN MARCH COMPARED TO REVISED FEBRUARY RATIO OF 1.93:1.

-- CONSUMER PRICE INDEX (NSA) ROSE BY 8.4 PERCENT TO 171.2 IN TWELVE MONTHS TO APRIL, AS FAVORABLE IMPACT OF CUT IN PROVINCIAL SALES TAXES OUTWEIGHED CONTINUED SHARP ADVANCE OF FOOD PRICES (OTTAWA 2540). AIB'S INDEX OF FOOD PRICES INCREASED BY 2.6 PERCENT BETWEEN MARCH AND

APRIL. FOOD INDEX STANDS AT 137.1 (1974=100), 11.9 PERCENT HIGHER THAN APRIL, 1977 LEVEL.

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-- CONSUMER CREDIT OUTSTANDING (NSA) REACHED CDOL\$ 25.1 BILLION IN MARCH, A 11.7 PERCENT INCREASE OVER MARCH 1977. CONSUMER CREDIT OUTSTANDING EXHIBITED TWELVE MONTH INCREASE OF 11.4 PERCENT AND 11.6 PERCENT IN FEBRUARY AND JANUARY RESPECTIVELY.

6. EXCHANGE RATE: CANADIAN DOLLAR EXCHANGE RATE HELD FIRM IN VICINITY OF 90 U.S. CENTS DURING WEEK. EARLY IN WEEK DOLLAR REACHED HIGH OF 90.35 U.S. CENTS, BUT FELL BACK TO 89.76 U.S. CENTS FOLLOWING STATEMENT BY QUEBEC FINANCE MINISTER PARIZEAU THAT A SOVEREIGN QUEBEC MIGHT HAVE AN INDEPENDENT MONETARY POLICY. DOLLAR RECOVERED SOMEWHAT WITH NEWS THAT INFLATION RATE DECELERATED IN APRIL AND CLOSED AT 89.98 U.S. CENTS FOR WEEK.

7. IN STATEMENT TO COMMONS COMMITTEE MAY 16, BANK OF CANADA GOVERNOR BOUEY SAID CANADIAN ECONOMY WAS NOW MORE COMPETITIVE WITH U.S. THANKS TO LOWER RATE OF NOMINAL WAGE INCREASES, BETTER CONTROL OVER GOVERNMENT SPENDING, CONTROL OVER MONEY SUPPLY, AND LARGE EXCHANGE RATE ADJUSTMENT. HE SAID AS RESULT CANADIAN CURRENT ACCOUNT DEFICIT MIGHT BE SMALLER THIS YEAR THAN LAST. HE ALSO SUGGESTED THAT FOREIGN EXCHANGE MARKET INTERVENTION BY CENTRAL BANK HAD NOT BEEN SYMMETRICAL DURING RECENT PERIOD OF SHARP DOWNWARD PRESSURE ON CANADIAN DOLLAR. TEXT POUNCHED; COMMENTS SEPTEL.

8. CAPITAL MARKETS: SHORT TERM INTEREST RATES CONTINUED TO EASE IN WEEK. INTEREST RATE ON 3 MONTH TREASURY BILLS WAS 8.07 PERCENT COMPARED WITH 8.13 PERCENT PREVIOUS WEEK.

9. TWO BANK RATE INCREASES THIS SPRING TOTALLING 100

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BASIS POINTS (ONE PERCENTAGE POINT) HAVE BEEN CRITICIZED BY MARKET ANALYSTS FOR NOT HAVING THEIR INTENDED EFFECT OF HALTING THE SLIDE OF THE CANADIAN DOLLAR IN MARCH AND APRIL. AS ADMINISTERED AND OTHER INTEREST RATES ROSE, EXCHANGE RATE DEPRECIATION CONTINUED, AND MARKET RATES HAVE BEGUN TO COME DOWN ONLY AS CANADIAN DOLLAR BEGAN TO SHOW MORE STRENGTH. IT APPEARS THAT INTEREST RATES HAVE

RESPONDED IN LARGE MEASURE TO EXCHANGE MARKET FORCES, RATHER THAN EXCHANGE MARKETS RESPONDING TO INTEREST RATES AND U.S./CANADIAN YIELD SPREADS AS THEY DID DURING MUCH OF 1976 AND 1977. YIELDS ON THREE MONTH CANADIAN TREASURY BILLS ROSE FROM 7.66 PERCENT IN EARLY MARCH TO A HIGH OF 8.24 PERCENT IN LATE APRIL AS THE CANADIAN DOLLAR SANK TO NEW LOWS, BUT YIELDS HAVE SINCE DECLINED AS THE DOLLAR RECOVERED. THE CURRENT RATE (SEE PARA ABOVE) IS ONLY 41 BASIS POINTS ABOVE LEVEL ON DAY BEFORE FIRST INCREASE THIS YEAR OF BANK RATE (MARCH 9). YIELD SPREADS BETWEEN U.S. AND CANADIAN THREE MONTH TREASURY BILLS MOVED FROM 140 BASIS POINTS IN EARLY MARCH TO 190 IN LATE APRIL, BUT HAVE SINCE FALLEN TO 179.

10. BOND PRICES MOVED UPWARD IN WEEK. SOME ANALYSTS FEEL, HOWEVER, THAT RECENT STRENGTH IN BOND MARKET IS ATTRIBUTABLE TO TEMPORARY FACTORS SUCH AS DEALER INVENTORIES, FLUSH CASH POSITION OF INSTITUTIONAL BUYERS, AND TO STRONGER CANADIAN DOLLAR. THUS, IT IS JUDGED THAT LONG TERM RATES COULD SOON BEGIN TO RISE.

11. HYDRO QUEBEC HAS ARRANGED CDOLS 500 MILLION LINE OF CREDIT WITH CHARTERED BANKS. HYDRO IS APPARENTLY HEDGING AGAINST POSSIBLE FINANCE DROUGHT NEAR TIME OF REFERENDUM.

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P 250240Z MAY 78
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12. FOREIGN BORROWING: FINAL TERMS SET FOR PROVINCE OF QUEBEC'S 30 BILLION YEN (CDOLS 150 MILLION) ISSUE. BONDS WILL HAVE 12 YEAR MATURITY, CARRY COUPON OF 6.4 PERCENT AND ARE PRICED AT 99.40 TO YIELD 6.48 PERCENT.

13. COST OF CANADIAN BORROWING IN EUROPE COULD RISE, IN PART DUE TO MONTH-LONG MORATORIUM ON FOREIGN BORROWING IMPOSED BY FRG. GOC 600 DM ISSUE IS UNDER WIRE, BUT PRICE OF BONDS HAS DECLINED ONE POINT FROM OFFERING PRICE. IT IS EXPECTED THAT UPCOMING ISSUES BY PRIVATE CANADIAN BORROWERS AND BY HYDRO ONTARIO IN EUROMARKET WILL SELL AT DISCOUNT. ENDERS

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